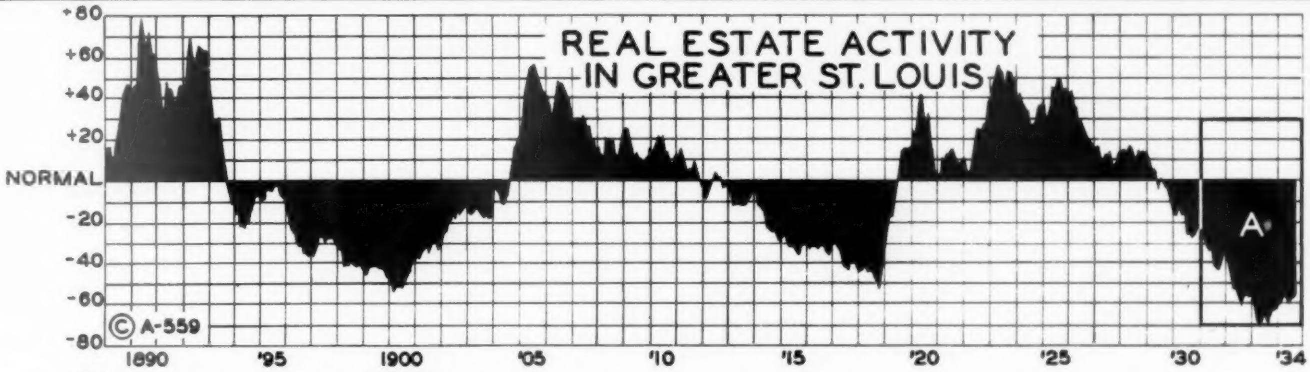
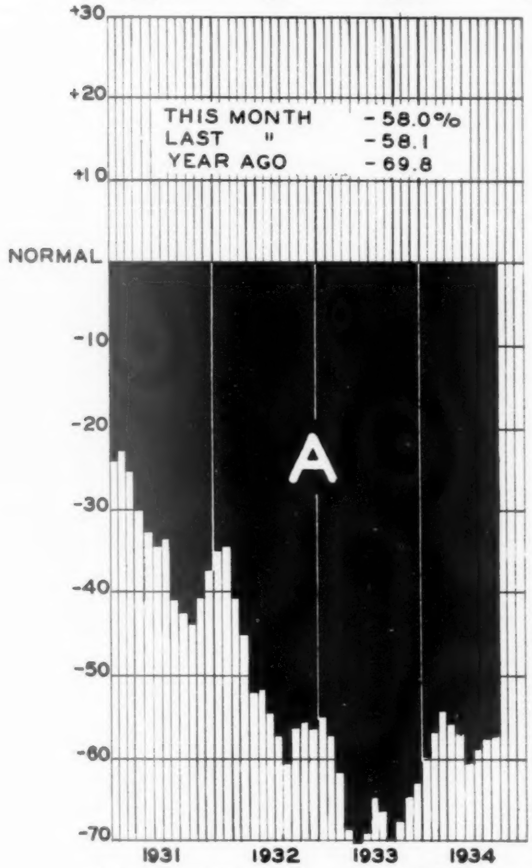
OCTOBER, 1934

The Real Estate ANALYST





RESIDENTIAL vacancies continue to disappear at a very rapid rate. In Saint Louis 1100 units were absorbed from September 5 to October 5. This absorption was particularly rapid in apartment units. Total residential vacancy in Saint Louis is now down to 5.6%.

The rapid absorption during the past month is more surprising in view of the general business situation. Gains have been quite slow during the summer, with the preliminary figures for September showing a slight recession. The Marriage rate, one of the most sensitive barometers of changes in the general business situation, shows a slight decline.

Real Estate Activity, as shown on the long chart above and the enlarged section to the left, shows an infinitesimal increase during the month. This too, is encouraging. The fact that a loss was not experienced is an indication that the moneyed public is gradually becoming aware of the attractiveness of real estate in comparison with other types of investments.

The foreclosure rate in Saint Louis showed a substantial drop during the month. It is now 43% below the corresponding month of a year ago.

Rentals of single family dwellings increased very slightly, while our index of apartment rentals showed a slight decline.

New residential building was 16% under a year ago. Modernizing and repair work in Saint Louis, in spite of the provisions of the National Housing Act, ended the month 31½% under a year ago. Building material prices declined very slightly during the month.

A housing shortage is inevitable, and those who buy residential real estate before this fact becomes generally known will realize the greatest profit. If the present rate of absorption continues, the shortage of dwelling units will be apparent to all within the next six months.

HOW HIGH WILL RENTALS AND VALUES GO?

THE Real Estate Analyst has, in numerous issues during the past year and a half, indicated the reasons for its belief that rentals and values would increase sharply during the next few years, until levels at least as high as those of the last boom are reached. With this forecast, many leading economists are in agreement. Dr. F. A. Pearson of Cornell University, generally acknowledged to be one of the leading authorities in the United States on price fluctuations, has characterized our forecast on rentals in the February, 1934 issue as "a masterly analysis of a complicated problem". We have, however, just received a copy of the report of the Philadelphia Housing Association for 1933. On page 8 we find this statement: "one thing is certain, there is little likelihood that in the life time of the present generation residential sales or rental values will reach the levels that existed during the boom period. The over valuing of Real Estate was possible only because an unusual combination of circumstances was present during the peak of the cycle. In fact, the available records indicate that only once within the past fifty years has the same combination of circumstances been present."

There can be no question about the difference of opinion in this case. Either the Real Estate Analyst is right or the Philadelphia Housing Association is right. The policy of all present owners of real estate depends to a very large extent on the selection of the correct forecast.

Our belief that rentals and values will equal or exceed the rentals and values of the last boom period is based on the fact that construction costs have advanced sharply during the past year and a half, and are certain to advance still further when building in any volume actually starts. The Philadelphia Housing association admits this increase. In fact they state in their report, "it is safe to assume that replacement costs are approximately the same today under the construction code as they were in 1925". (We do not believe this is yet a safe assumption.)

This increase in construction costs has started a chain of events which will inevitably bring higher rentals and values. The sequence of events in this series is as follows:

(1) Cessation of Building. With residential rentals 37% below the 1925 level (U. S. Bureau of Labor Statistics for Principal Cities), with real estate taxes 25% above the 1925 level, with decorating and repair work required in excess of normal requirements due to a tenant's market, real estate has become exceedingly unprofitable. This in itself, and through causing heavy foreclosures with the consequent dumping of distress properties on a disinterested market, has forced values and rentals to a point where the incentive to build is no longer present. The Philadelphia Housing Association does not seem to understand the necessity for this incentive. They accuse the mortgage and real estate interests of deliberately conspiring to prevent new building with the purpose of increasing values of present buildings. Ordinary business judgment on the part of contractors, real estate operators or financial agents prevents the building of houses which on completion will not sell for enough to repay their cost of construction, nor rent for enough to pay a return on the investment required.

(2) Absorption of Vacancy. In spite of the cessation in building which came rather early in the depression, vacancy increased steadily as a larger and larger percentage of families were forced to give up separate living quarters due to unemployment and economic distress. At the same time many of the older family units were being dissolved by death, while the retardation of the marriage rate due to economic uncertainty prevented the formation of new family units to take the place of those dissolved. This latter cause alone, at the bottom of the depression, was reducing the number of separate family units by more than one percent per year. As a result of these causes, residential vacancy in the early months of 1933 in urban areas of the United States was averaging from twelve to fifteen percent.

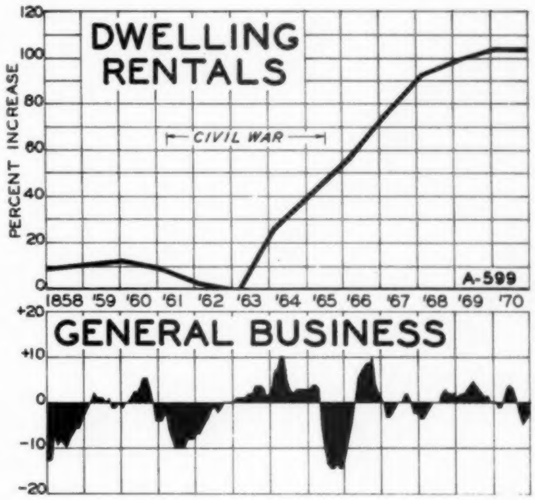
Vacancy would have increased still further had not the demolition of many of the more obsolete buildings more than offset the few additional dwelling units built during this period. The Philadelphia Housing Association reports that in Philadelphia, during the past four years, 3809 new accommodations were built, while 4317 old accommodations were demolished.

The improvement in industrial conditions which has come since then has reversed these processes until now vacancy is being absorbed at a rate at least as rapid as the rate at which it formerly increased. In Saint Louis residential vacancy has fallen from 13% in the early months of last year to 5.6% on the fifth of this month. This absorption of units will continue until a housing shortage develops.

(3) Increases in Rentals. There is no question in our mind but that a housing shortage will cause rentals to increase sharply. The reduction in vacancy which we have already experienced has caused our barometers on Saint Louis residential rentals to turn up slightly during the past few months. As the housing shortage becomes acute rentals will skyrocket.

(4) Increase in Values. As vacancy drops and rentals rise the net income from real estate increases rapidly. This increases its desirability as an investment. At the same time tenants, grown arbitrary during the depression, are faced with landlords who have lost enough of their docility to make the tenants appreciate the advantages of being their own landlords. They start to question the statement that it is cheaper to rent than to own.

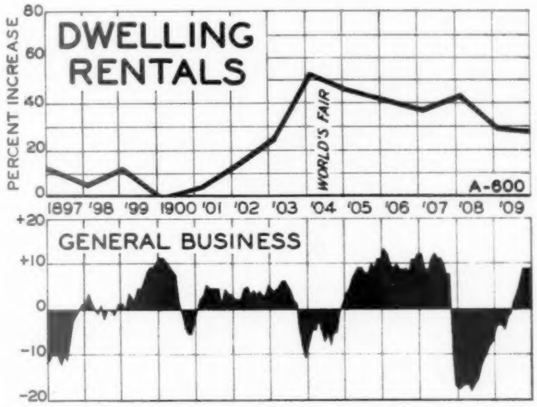
The Philadelphia Housing Association report questions the probability of radical rental increases because of the inability of the tenant to pay a larger amount. It points out that during the last rapid increase in rentals, "the demand for houses came from a prosperous people". It apparently doubts that recovery will be sufficient to support higher rentals. In an effort to determine as much as we could about business conditions which preceeded the other rapid rental increases we have had in Saint Louis during the past eighty-five years, we have charted these increases in comparison with the cycles of production activity as computed by Colonel Leonard P. Ayres.



The chart to the right shows the rapid increase in rentals which occurred during and after the Civil War. Rentals more than doubled although it is quite apparent from the lower chart that this was not a period of unusual prosperity. The depression in '65 apparently had no effect in halting the upward movement.

The real reason for this increase in rentals was the increase in building costs caused by the green-back inflation. This stopped building, creating a housing shortage. Building was not resumed until rentals rose sufficiently to apparently pay a return on the new cost of construction.

The second major increase in rentals during the past eighty-five years in Saint Louis started in 1900 and culminated at the time of the World's Fair in 1904. While there was a slight upward movement during this period in general prices, including the cost of building, this increase in rentals was primarily due to the releasing of the dammed up demand accumulated during the depression of the nineties. Following this depression, the marriage rate increased 60%, and the families occupying dwelling units with other families expanded to separate quarters. Had this expansion of demand been accompanied by large increases in construction costs no new building would have taken place, and rentals would have advanced by more than the 50% shown on the chart.

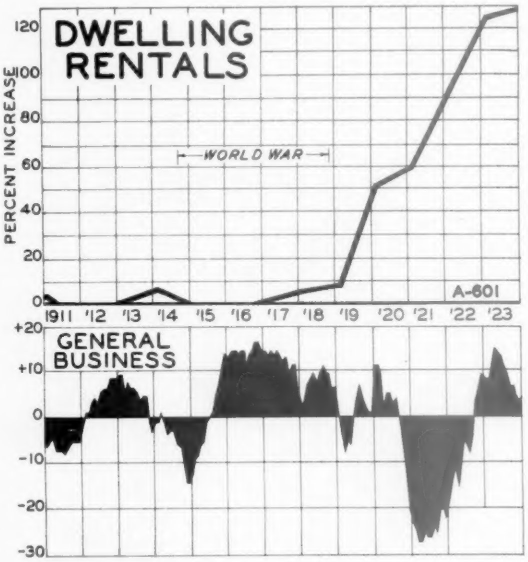


The third major rise in rentals occurred immediately following the World War. (This is shown on the chart on the following page.) In $3\frac{1}{2}$ years rentals more than doubled, and in 5 years they increased by 125%. This is the period which the Philadelphia Housing Association refer to in their statement when they said "over valuing of real estate was possible only because an unusual combination of circumstances was present during the peak of the cycle. In fact, the available records indicate that only once in the past fifty years has the same combination of circumstances been present".

The only combination of circumstances we know of responsible for this tremendous increase in rentals and values was the increase in construction costs. From 1913 to 1925 the combined labor, material and overhead cost of erecting a residen-

tial building increased by more than 82%. This increase, particularly rapid during 1918-1920 halted all new building, and the expansion of demand which followed the clearing up of the uncertainties of the war developed a drastic housing shortage.

It is rather interesting to note the relationship of general production activity as charted by Colonel Ayres and this increase in residential rentals. The period in which rentals were advancing most rapidly was the period in which, according to Colonel Ayres, industrial activity was much below normal. This is shown very strikingly on the chart to the left.



The chart of general business activity in Saint Louis on pages 320-321 in this issue does not show these years below normal. but neither does it show the general postwar prosperity as starting until after rentals had made the greater part of their gain.

In many communities in the East the depression of 1920 and 1921 was quite severe. The figures of the United States Bureau of Labor Statistics show that rentals in eastern cities underwent the same increases experienced in Saint Louis during these years.

One other factor which we believe the report of the Philadelphia Housing Association does not take into consideration is that the percentage of family income which is paid in rent varies considerably at different times in the business cycle. This was discussed and charted in the August issue of the Real Estate Analyst. It will be recalled that at the present time the percentage of wages paid in house rent is the smallest on record, 43% less than the amount in 1913. The fact that rentals are almost back at prewar figures while wages are still considerably above makes this self evident.

We are certain that the eventual level of rentals and values will be determined almost entirely by the eventual level of replacement costs. The March, 1934 issue of the Real Estate Analyst charted building material costs in relation to rental levels for eighty-four years, showing that over this entire period the general trends have been identical. Every rapid rise in building costs has been followed later by a comparable rise in rentals, restoring the old relationship of the two lines.

Since this is true, our problem of how high rentals and values will go during the next few years resolves itself into the question of how high replacement costs will go. Certainly they will go much higher than they are now as building in any quantity is again resumed. Our studies lead us to believe that building costs will exceed the costs during the last boom. The savings in financing costs under the National Housing Act will not be sufficient to offset this increase. This was discussed in detail in the July issue of the Real Estate Analyst.

If building costs go as high as our studies lead us to believe, then rentals must at least double before there is much incentive to build.

Let us frankly face the fact that the impossibility of stimulating the building industry at the present time will result in a slower recovery than we would otherwise experience. A large percentage of the unemployed at present were formerly employed in either the construction field or in industries manufacturing or transporting construction materials. However, in the lagging of the construction industry in recovery this depression is no different from most of the great depressions we have experienced. Recovery has always come first in the lines where demand is not very elastic. The purchase of most capital goods is optional at any particular time and is rarely contracted for unless sufficient incentive is present.

ROGER BABSON ON REAL ESTATE

IN addresses and reports recently, Roger Babson advocated the purchase of real estate. With this advice we agree. Since we left the gold standard the Real Estate Analyst has constantly urged its clients to buy real estate. Wisely selected at present prices it should yield a substantial profit in the next few years.

Here our agreement with Mr. Babson ends. According to press reports, he believes that "vacant ground suitable for building" will show the greatest percentage of increase in value. We do not so believe. The value of potential building lots depends on: (1) Demand, (2) Supply, and (3) the general price level.

With residential building proceeding at only 5% of its accustomed level the demand for building sites has reached a low ebb. Mr. Babson evidently expects a sharp reaction. We expect only a slight improvement during the next year.

Many factors should increase the demand for building lots. Among these are the return to the cities of many of those who left during the depression, the spreading out to individual dwelling units of families living with other families because of economic distress and the accelerated depreciation and obsolescence of older buildings neglected during a period of insufficient earnings. Also, during this entire period, blighted areas in the older districts of the cities have continued to grow, causing these cities to die at the center and grow at the periphery.

At the present time the demand for dwelling units is increasing faster than the supply, with a housing shortage imminent. The marked reduction in dwelling vacancies has caused rentals to increase, and has stopped the decline of values.

What will be the probable supply of building sites in the next ten years?

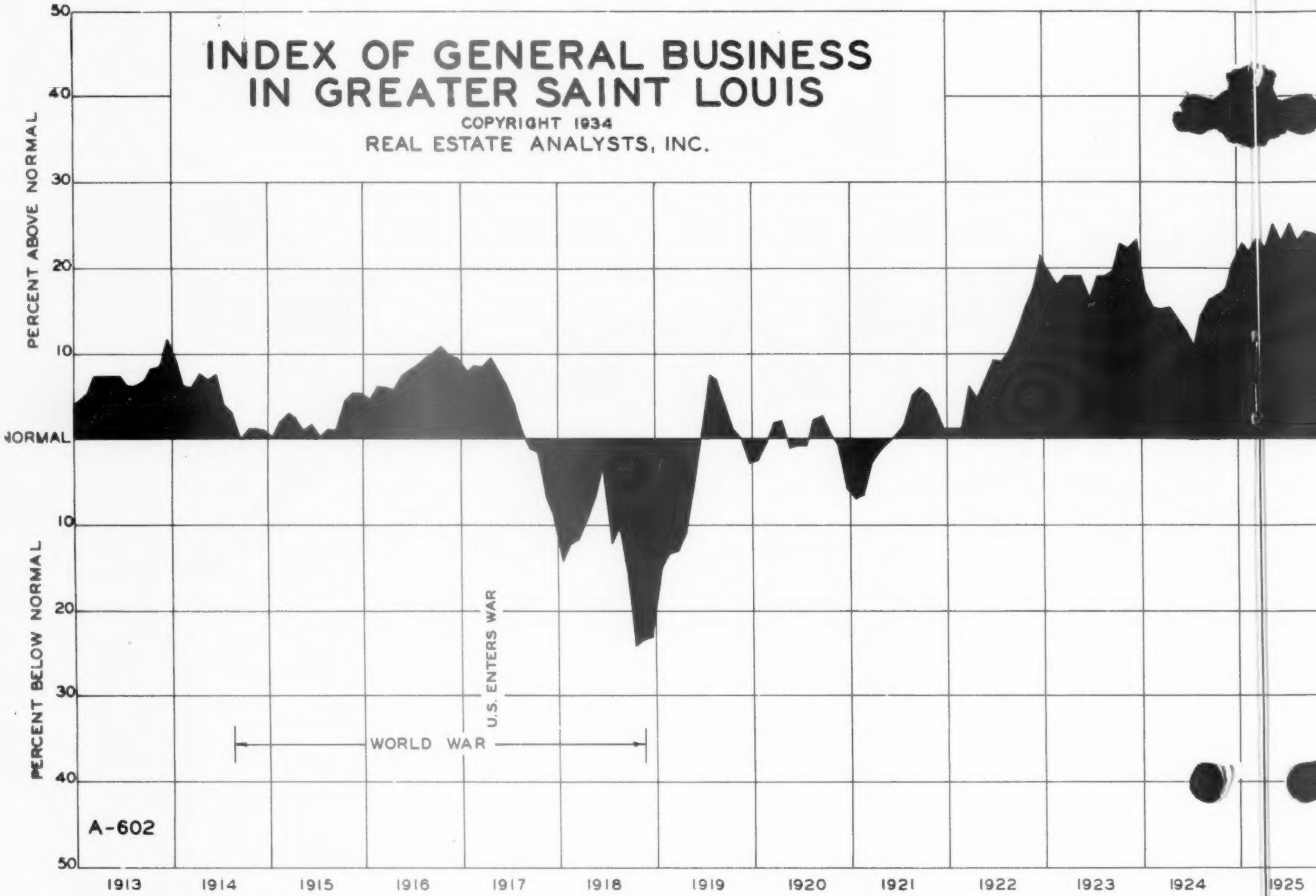
Toward the end of the last boom, an excess of subdivision activity glutted the market. A survey of the Saint Louis Regional Plan Association shows that in that portion of Saint Louis County adjacent to the limits of Saint Louis there are at present, already subdivided, 61,407 vacant lots. These lots would accommodate a population 30% larger than the present total population of Saint Louis County. There is also unsubdivided property in this area practically equal to the area of the lots already subdivided but unused. Much of this ground, prior to the present depression, was not accessible because of a lack of roads and streets. In an effort to create employment, semi-urban areas around all large cities have been strewn with a network of hard surfaced roads and streets. It should be remembered that every mile of street laid in a semi-urban area makes accessible two additional miles of frontage.

A decade ago relatively little frontage in territory adjacent to a city was accessible enough for building sites of average value. Suburban land which was accessible was relatively high in price. The development of new roads and streets will reduce the relative value of many of the older sites, and increase the value of much of the new frontage. The foregoing facts, in addition to the probability of little residential building in the United States during the next year, lead us to believe that values of building lots will not increase as much as many types of improved real estate.

The revaluation of the dollar in gold is having the effect of raising all prices in our lighter dollar. All types of real estate will share in this appreciation.

Mr. Babson is also quoted as saying that "there will be a heavy depreciation in buildings already constructed due to radical changes, new inventions and customer demands". This forecast is based on the belief that construction methods will be greatly improved, resulting in a home superior to the present conventional type, without a cost greater than present construction methods. We are convinced, that new methods of construction will replace the present archaic methods. Rapidly increasing building costs, both of labor and materials, under existing codes will accelerate this shift. We are convinced, however, after a detailed study of new materials and pre-fabricated units, that the wide spread use of new methods and materials will come very slowly.

On the other hand, current replacement costs are considerably above present prices of improved real estate. These costs will advance still further due to wage increases under the codes. They will not be offset sufficiently by savings in financing under the National Housing Act. This will eventually result in an appreciation of present buildings, during the next five years, which will be far greater than appreciation of building sites. We believe that apartment properties have been forced to lower levels than other types of property, and will therefore show the largest percentage of rebound.

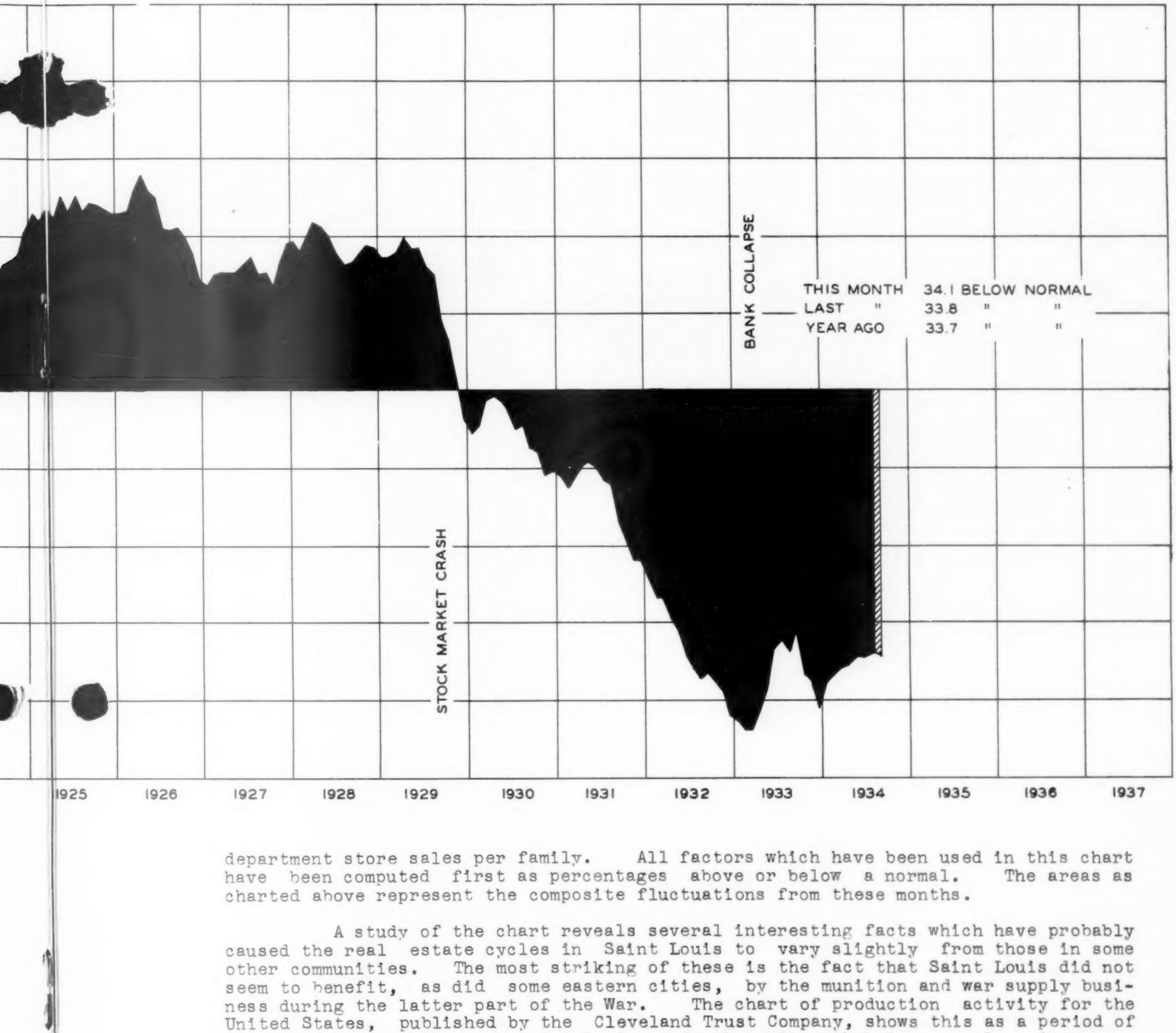


GENERAL BUSINESS CONDITIONS AND REAL ESTATE

IF there is any value in the studies made during the past few years by Real Estate Analysts, Inc., it lies largely in the fact that for a single representative city it has reconstructed on a measured basis by months for from twenty to eighty years, all of the factors which affect real estate. A complete study of a single city, we believe, is of greater value in determining the causes and effects of fluctuations of real estate than would be a superficial study of many cities based on the meager data available prior to the last few years.

The fluctuations of general business activity in Saint Louis is a factor we have not previously presented in the Real Estate Analyst. Its importance in modifying the real estate cycle is too great to be ignored.

The chart shown above is the result of an effort we have made to measure what the average business man calls "business conditions". It is a composite of various barometers, each selected because it measured in a general way some type of local business activity. Every effort has been made to correct all of the figures used for seasonal fluctuations, for price changes, for the growth of the city and for other miscellaneous factors. As an example of the complicated problems involved it was necessary to correct the dollar total of all check transactions for price changes. As check transactions represent a combination of wholesale and retail transactions, wage payments, payments of taxes, purchases of securities, interest and principal payments and multitudinous other things, it is quite apparent that the correction used for changes in the general price level must take into account the lag which occurs in changes in many fixed items as well as the more rapid changes which take place in wholesale purchases. A different price correction was used on

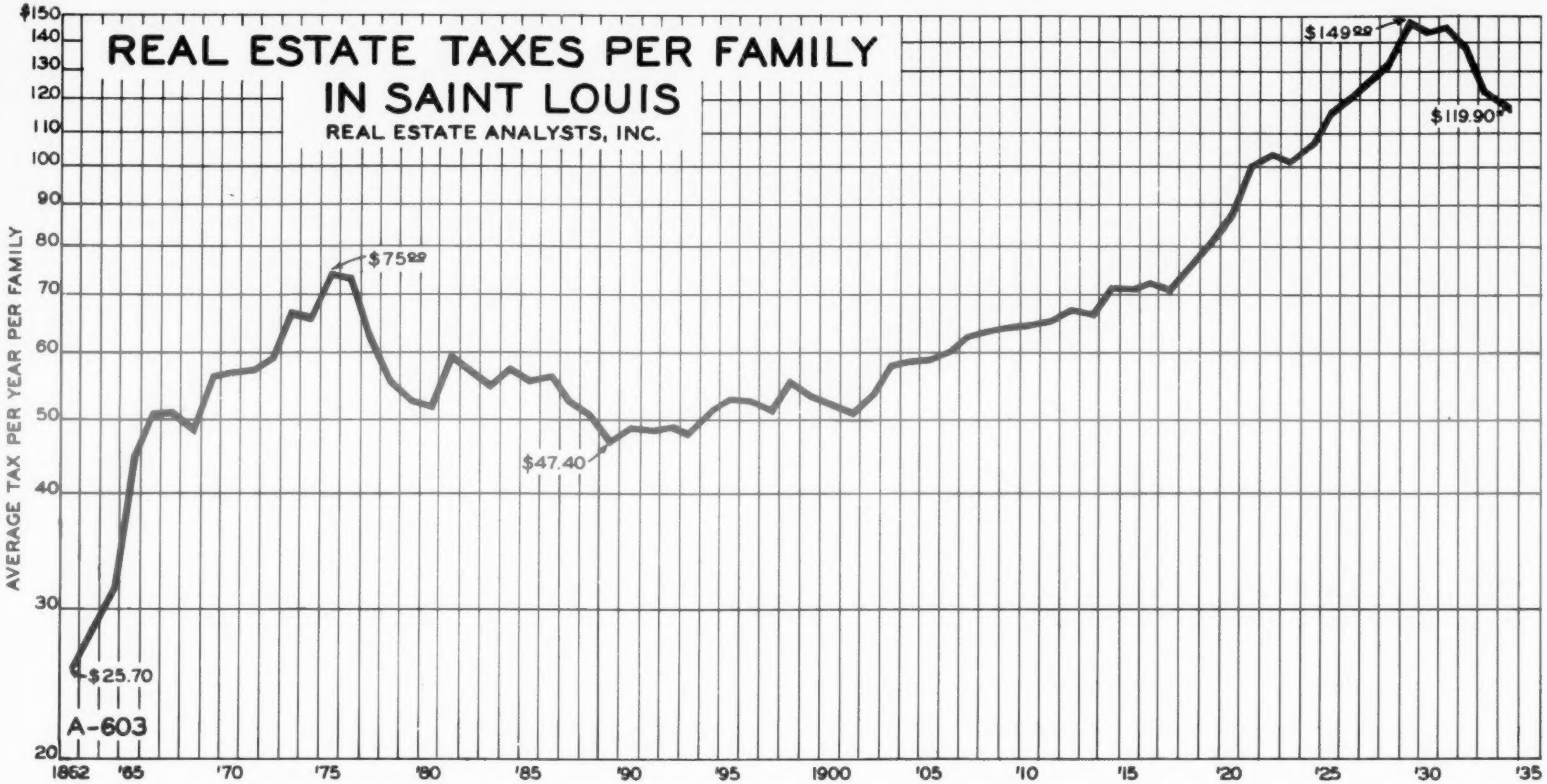


department store sales per family. All factors which have been used in this chart have been computed first as percentages above or below a normal. The areas as charted above represent the composite fluctuations from these months.

A study of the chart reveals several interesting facts which have probably caused the real estate cycles in Saint Louis to vary slightly from those in some other communities. The most striking of these is the fact that Saint Louis did not seem to benefit, as did some eastern cities, by the munition and war supply business during the latter part of the War. The chart of production activity for the United States, published by the Cleveland Trust Company, shows this as a period of great activity, while our Saint Louis study shows it much below normal. As a compensating factor, however, Saint Louis did not experience the severity of the depression of 1920 and 1921, shown on the Cleveland Trust Company study as the deepest of all depressions prior to the present. During the later twenties, prosperity in Saint Louis was apparently greater than it was in other parts of the country. The drop culminating in the bank collapse in the spring of 1933 did not carry business in Saint Louis to near the depths shown on the national study.

There seems to be only slight agreement between this chart of general business activity prior to 1922 and the chart of real estate activity prior to 1922. From that time on, however, the agreement is fairly close. (See the chart of real estate activity on the front page.)

The shaded area at the right end of the chart represents the preliminary figure for the past month. While this figure is below the preceding month and below a year ago, it is much above the figure of last December. After losing much of the gain of the earlier part of last year, business seems to have been making slow but very steady gains since last December.

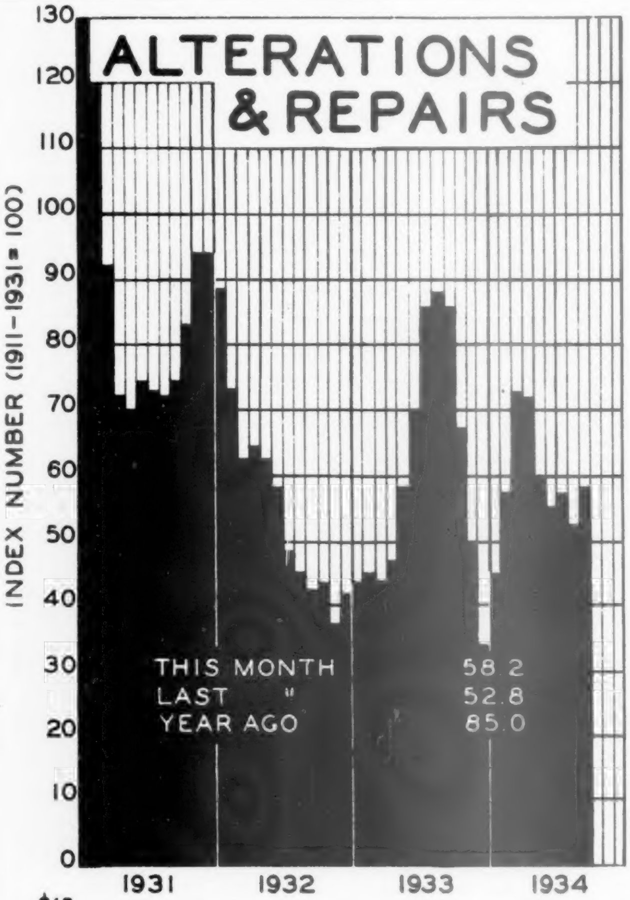


THE chart above shows a variation in the average real estate tax per family in Saint Louis from 1862 to the present. It will be noted that during the Civil War and in the period immediately following, the average tax increased from $25.70 per family to $75, or 171%. As long as the post Civil War boom continued, all went well; but as the great panic which started in 1873 got well under way, real estate activity ceased, foreclosures started mounting and a situation developed which was very similar to the one in which we have found ourselves during the past few years. Popular clamor at the time called for a reduction in taxes, which resulted in a drop of 31% from the peak in five years. This chart was printed originally in the April, 1932 issue of the Real Estate Analyst. In that issue we stated "we believe it entirely within the range of possibility that within the next four or five years reduction in real estate taxes will approximate the reduction after the post Civil War boom". It will be noticed from the chart above that thus far taxes have been following closely in accord with our forecast.

Another factor has entered the picture now in the revaluation of the dollar which will prevent very much of a further reduction. We believe that within a few years' time taxes will again start mounting, as general prices of services, commodities and real estate rise.

THE chart shown above is drawn from index numbers compiled by the Federal Employment Stabilization Office in Washington. These index numbers show the relative employment in the production of structural steel, cast iron pipe, cement, mill work, steam fittings, and brick, tile and terra-cotta. These figures have been corrected for seasonal fluctuation. They represent, we believe, one of the best indexes of the variation in the demand for building materials, as price changes destroy the value of most barometers based on dollar figures.

It is rather interesting to note the very rapid decline following the stock market collapse. As investment in new construction is almost always optional at any given time, it is generally postponed when a lack of confidence in the future or a decrease in the probable return makes it apparently inadvisable. The low point of 29.6% of the 1923 to 1925 average was reached at the time of the bank collapse in March, 1933. The August, 1934 figure, which is the latest figure available, is 41.1% of the 1923 to 1925 average. We expect this line to climb very slowly during the next year, after which it should rise more rapidly. This chart will be kept up-to-date in our office, and reprinted in the Real Estate Analyst whenever significant changes occur.

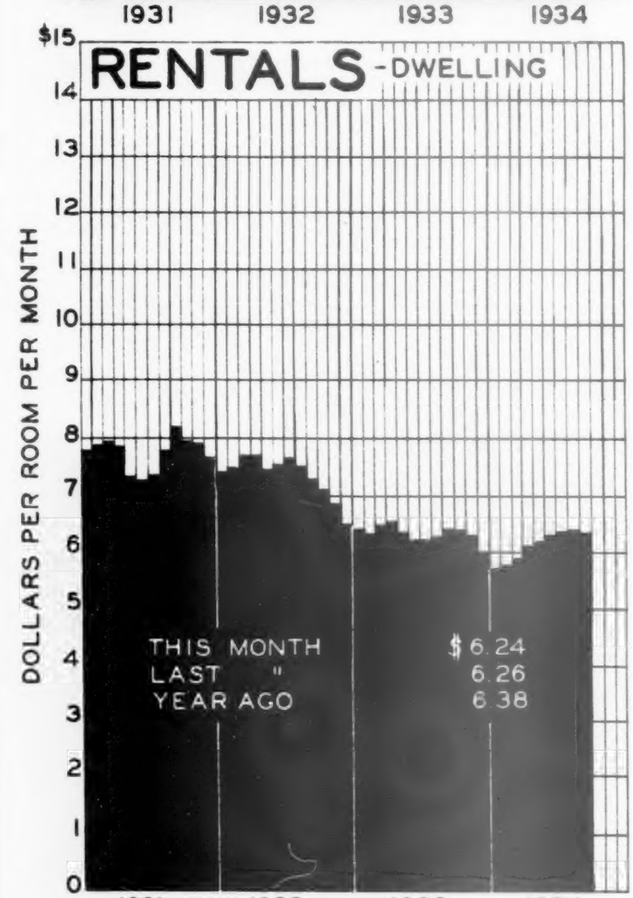


The chart to the left shows the volume of modernizing and repair work done in Saint Louis each month for the past four years. This chart will carry on the figures given in the long chart on pages 308-309 in the September issue.

This index, as explained in the article in that issue, has been adjusted for seasonal fluctuation, changes in the cost of making repairs, and the growth of the city.

A study of the complete chart extending back to 1911 seems to indicate that the volume of repair work in the past has depended largely on the general business situation. The peak last year accompanied the very rapid increase in general business. The business recession of last fall had a dampening effect on repair work.

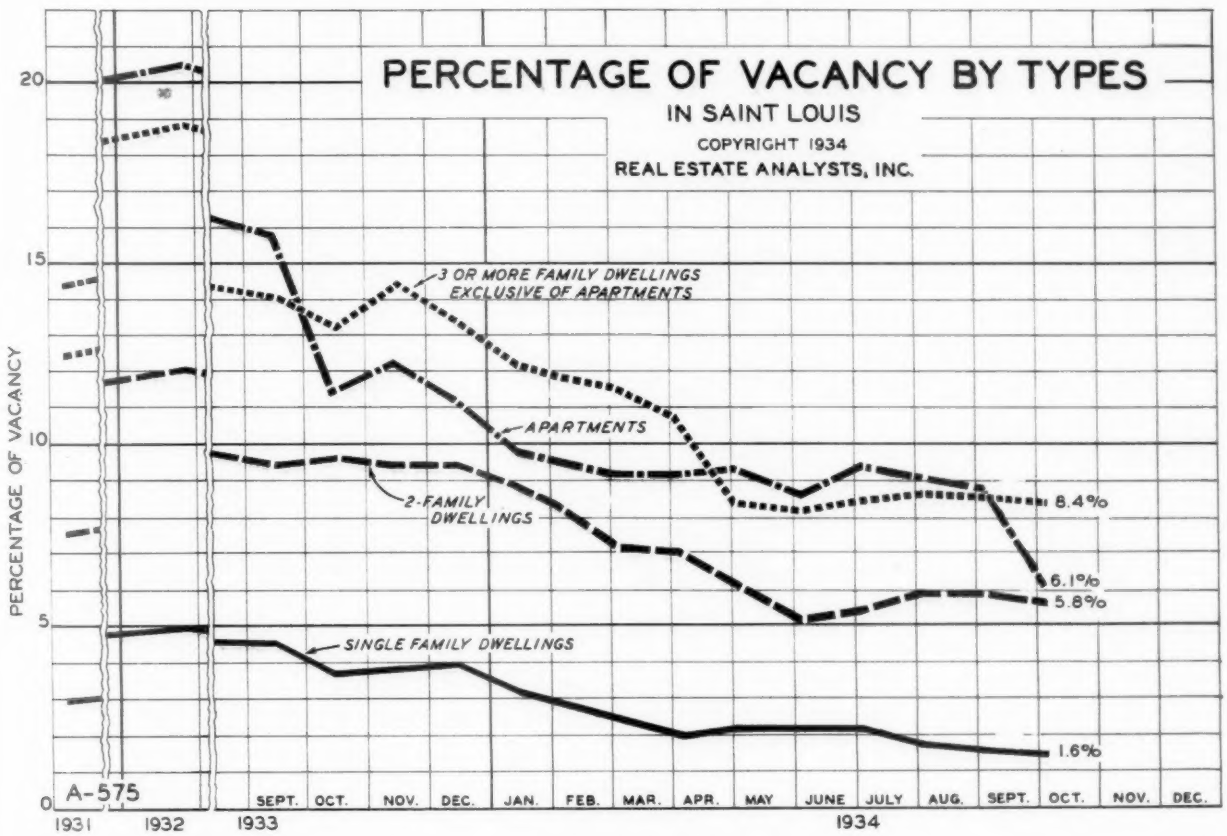
We believe that if general business attains a fair degree of recovery this fall, the modernizing and repair campaign under the National Housing Act will attain a fair degree of success. If recovery drags, its success will not be spectacular.



The chart to the left shows the index of advertised rentals on four, five and six room dwellings. The somewhat similar chart on the back page of this issue includes all types of single family dwellings, many of them of the older, more obsolete variety with a larger number of rooms.

It will be noticed that rentals of four, five and six room dwellings have advanced further since this last January than has the average of all single family units.

Rather peculiarly, during the month of September, the average of all single family dwellings as shown on the chart on the back, advanced by five cents a room while the four, five and six room quarters dropped two cents. Slight advances and declines of this amount are not significant. We believe that in the relatively near future increases will be seen of really significant size.



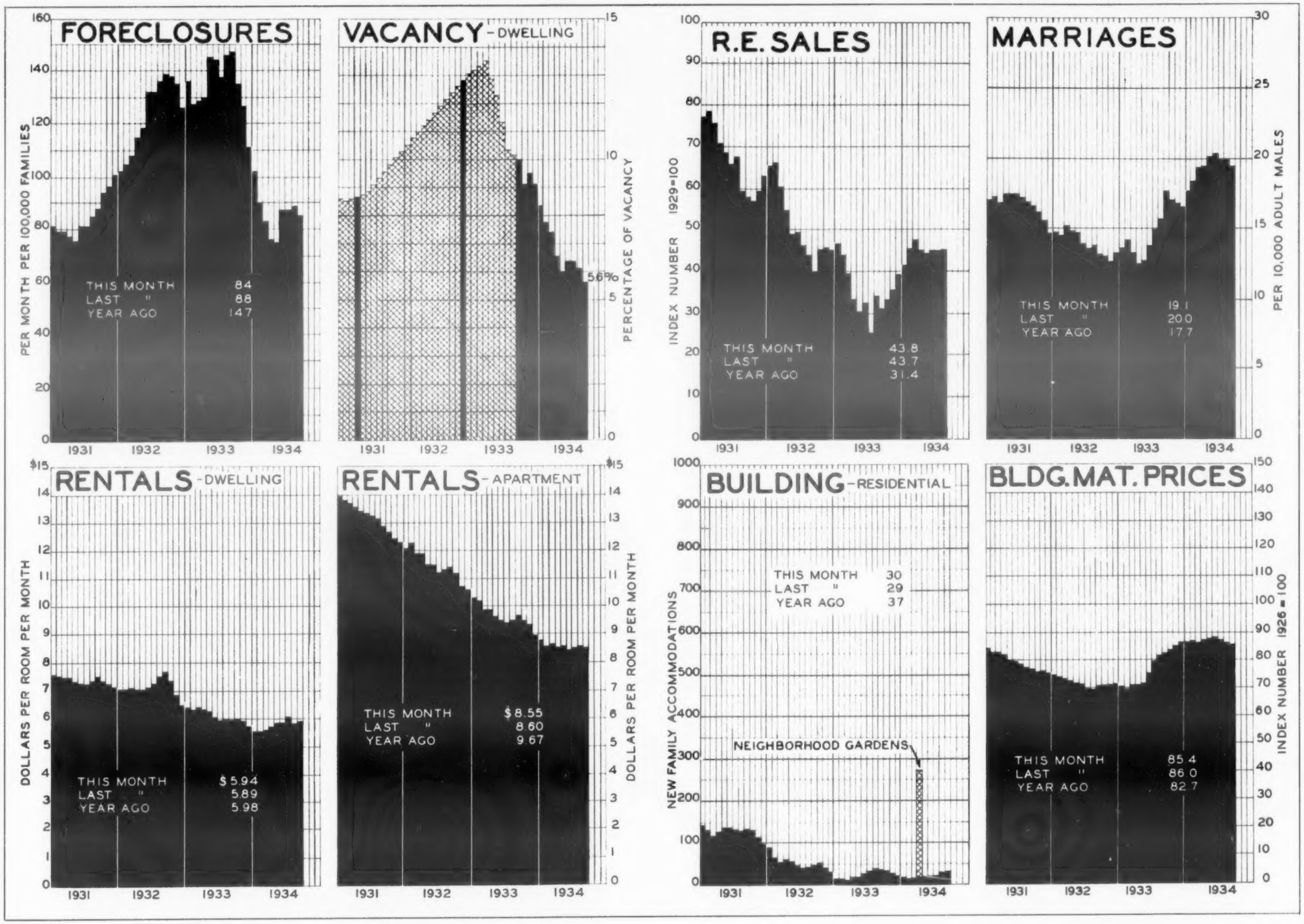
THE chart above shows the drop in residential vacancy in Saint Louis by types of units. The most significant development in recent months is the reduction in apartment vacancy. It will be noticed that the same rapid absorption took place a year ago in this type of unit. We also think it quite significant that this decrease in apartment vacancy was not accompanied by an increased vacancy in other types of units. It therefore represents a net gain and not merely a shifting from houses and "flats" to apartments.

The number of vacant units in Saint Louis by months since the introduction of the monthly vacancy survey by Real Estate Analysts, Inc. is shown in the following table.

Month	Vacancy	%	Absorption
September '33	23,354	10.4	894
October	22,460	10.0	2,010
November	20,450	9.1	-900
December	21,350	9.5	1,102
January '34	20,248	9.1	1,598
February	18,650	8.3	1,100
March	17,550	7.8	900
April	16,650	7.4	1,950
May	14,700	7.5	1,200
June	13,500	6.0	-500
July	14,000	6.3	0
August	14,000	6.3	400
September	13,600	6.1	1,100
October	12,500	5.6	
Absorption in thirteen months			10,854

In addition to the monthly figures above we know that in November, 1932, residential vacancy totaled 28,207 units, or 12.8%. Vacancy has been reduced since then by 15,707 dwelling units.

It can readily be seen that it will not be necessary for absorption of vacant units to continue much longer to make this situation acute. When this time comes, rentals will rise very rapidly. As income from property increases, values will rise sharply.


FORECLOSURES
PER MONTH PER 100,000 FAMILIES
THIS MONTH 84
LAST " 88
YEAR AGO 147
VACANCY-DWELLING
PERCENTAGE OF VACANCY
5.6%
R.E. SALES
INDEX NUMBER 1929=100
THIS MONTH 43.8
LAST " 43.7
YEAR AGO 31.4
MARRIAGES
PER 10,000 ADULT MALES
THIS MONTH 19.1
LAST " 20.0
YEAR AGO 17.7
RENTALS-DWELLING
DOLLARS PER ROOM PER MONTH
THIS MONTH $5.94
LAST " 5.89
YEAR AGO 5.98
RENTALS-APARTMENT
DOLLARS PER ROOM PER MONTH
THIS MONTH $8.55
LAST " 8.60
YEAR AGO 9.67
BUILDING-RESIDENTIAL
NEW FAMILY ACCOMMODATIONS
THIS MONTH 30
LAST " 29
YEAR AGO 37
NEIGHBORHOOD GARDENS
BLDG. MAT. PRICES
INDEX NUMBER 1926=100
THIS MONTH 85.4
LAST " 86.0
YEAR AGO 82.7
1931 1932 1933 1934